

INTERNAL REVENUE SERVICE

Midstates Region

Date: FEB 15 1996

Department of the Treasury

Appeals Office

**55 North Robinson, Suite 939
Oklahoma City, Oklahoma 73102**

Person to Contact:
[REDACTED]

Telephone Number:
[REDACTED]

Key District: Dallas

Years: 1994, 1995

Dear Sir:

We considered your appeal of the adverse action proposed by your key District Director. Your exemption from Federal income tax under Section 501(c)(6) of the Internal Revenue Code is denied. Your denial was based on the fact that your primary purpose was to provide particular services to your members in form of healthcare insurance.

You are required to file Federal income tax returns on Form 1120 for the above years. You should file these returns with your key District Director, EP/EO Division, within 60 days from the date of this letter, unless a request for extension of time is granted.

You may direct questions about the decision to the appeals officer whose name and telephone number are shown above.

Sincerely,

[REDACTED]
Associate Chief, Appeals

**Internal Revenue Service
Midstates Region**

**Department of the Treasury
Appeals Office
4050 Alpha Road 5th Floor
Dallas, Texas 75244-4203**

Person to Contact:
[REDACTED]

Telephone Number:
[REDACTED]

(Not Toll Free)

**Refer Reply to:
8000 NWSA:BAG:bg**

Date:

January 9, 1996

Dear [REDACTED]:

I apologize for the length of time it has taken me to return to this case. I received the administrative files for the two organizations we last corresponded about. I have reviewed those files and will include these in the discussion of the issue in this letter. The determination I have reached through review and further research is that the hazards of litigation to the Government are minimal in sustaining the District Director's proposed denial of the organization under section 501(c)(6) of the Internal Revenue Code.

Section 1.501(c)(6)-1 of the Income Tax Regulations defines a business league as an association of persons having some common business interest the purpose of which is to promote such common interest and not to engage in a regular business of a kind ordinarily carried on for profit. Its activities should be directed to the improvement of business conditions of one or more lines of business as distinguished from the performance of particular services for individual persons. An organization whose purpose is to engage in a regular business of a kind ordinarily carried on for profit, even though the business is conducted on a cooperative basis or produces only sufficient income to be self-sustaining, is not a business league.

The District office's reasons for denying your tax exempt status is that you are performing particular services for individual members. Your membership consists of business employers engaged in different trades, occupations and professions rather than being limited to a specific industry. Your health plans and insurance services constitute a kind of business ordinarily carried on for profit and as such you are competing with profit entities that sell or underwrite healthcare policies.

Your purpose in part, as reiterated in your bylaws, is to bring together a cooperative group of Service Area employers to investigate and develop a purchasing cooperative for health care. Your purposes also include the research and gathering of data to develop recommendations for the improvement of the cost, quality, and access of health care for members as well as education of health care issues to members and the public. In your appeal you state that your goals are to provide better quality and lower-

cost healthcare to all persons in [REDACTED], including those who do not currently have, and cannot get, healthcare.

In Contracting Plumbers Cooperative Restoration Corporation vs. U.S., 33 AFTR2d 74-403, a contracting plumbers cooperative restoration corporation was determined not to be exempt under section 501(c)(4) or 501(c)(6). The taxpayer's sole purpose was to insure the efficient repair of "cuts" made in the streets of New York City by its members in the course of their plumbing activities. As the Second Circuit court stated in this case, "While we believe that taxpayer's activities are totally commendable, we nevertheless find that Congress has imposed certain limitations ... and that taxpayer simply does not qualify."

While your organization most certainly is beneficial, particularly to those businesses that would not otherwise be able to provide healthcare benefits to their employees, it is providing a particular service to its membership thus precluding it from exemption.

In MIB v. Comm., 84-1 USTC 9476, an insurance industry organization that collected and exchanged confidential underwriting information about applicants among member companies didn't qualify as an exempt business league. The Commissioner denied MIB's application stating that its business violated the requirements of the application regulation in two respects. First, the conduct of the information exchange constituted a "particular service" to MIB's members; and second, MIB was engaged in the kind of business ordinarily carried on for profit.

With regards to the first issue, the court determined that the information exchange constituted a particular service. The court stated that, "While it may be that the availability of such individual services also confers a general benefit upon all members and acts in the collective interest as a deterrent, it remains inescapable that the services being performed are all "particular services for individual persons." The court stated with regards to the second issue that because the organization did not qualify on the "particular service" ground it saw no need to consider this separate issue.

As in your case the availability of healthcare insurance to all members, whether large and able to obtain insurance on their own accord, or small and unable to be insured, acts to confer a collective benefit among all your members. This does not negate the fact that "particular services" are being provided for individual members.

You cite Independent Insurance Agents of Northern Nevada, Inc. v. U.S., 44 AFTR2d 79-5880 in support of exemption under 501(c)(6) of like organizations. In that ruling a business league won a refund of taxes paid on income that was characterized as income from unrelated business income from insurance premiums. The organization in this case was formed to advise and counsel tax supported governmental agencies within the State of Nevada with regard to insurance programs and to accept and service insurance written by such agencies for the purpose of

removing the placement of such business from political favoritism or influence and for effecting suitable coverage at the lowest ultimate cost to the taxpayer. The court stated, "It seems plain to us that the public service of managing the insurance needs of tax supported public agencies is an exempt purpose qualifying plaintiff as a business league under section 501(c)(6). The income realized is certainly related to the exempt purpose." Plaintiff corporation clearly is not "devoted to the promotion of a particular product at the expense of others in the industry. Its expressed and proved designed was and is "to assist its members and its industry in dealing with mutual business problems."

This case involved a clearly defined industry in which everyone participated in an effort to improve the industry. Your organization is made up of any business who wishes to take advantage of purchasing healthcare insurance by being part of a larger group. Only paid members benefit and only insurance companies which are selected by the Coalition can participate.

There are numerous revenue rulings cited in the District's proposed denial letter as well as in your appeal. I will attempt to analyze those which in my opinion are precedential in this case.

Revenue Ruling 70-641, C.B 1970-2, 119, involved an organization whose membership was open to persons engaged in various professions in the field of public health and welfare. These persons were united for the purpose of promoting a common business interest and improving their business conditions by exchanging knowledge and information in the field of public health and welfare and the improvement of professional services techniques. The organization's activities consisted of holding seminars, lectures, symposia, and discussions to provide an interdisciplinary forum for the exchange of ideas.

This revenue ruling was compared to Revenue Ruling 59-391, C.B. 1959-1, 151, which held that an organization composed of individuals, firms, associations, and corporations, each representing a different trade, business, occupation, or profession, was not exempt under section 501(c)(6). It was organized for the purpose of exchanging information on business prospects and its members had no common business interest other than a desire to increase their individual sales.

While I believe that some aspects of your organization, i.e. research and analysis, education of members and the public, fit within the scope of those purposes determined to be exempt in Rev. Rul. 70-641, your primary purpose for gathering such data is to be used to purchase health care on a cooperative basis. These educational aspects were the underlying purpose for the formation of the two entities we last corresponded about.

Both these organizations were membership organizations which developed educational programs to inform members and the public on health care cost management, health care management, and health care in general. They were exclusively educational and were granted exemption under section 501(c)(3).

In Revenue Ruling 71-155, C.B. 1971-1, 152, a nonprofit association composed of licensed insurance companies that made insurance available to persons who were in high-risk categories and could not otherwise obtain coverage qualified for exemption under section 501(c)(6). The State Insurance Commission required that all insurance companies writing the specified type of insurance be members. The purpose of the organization was to provide for the equitable distribution of high-risk policies among all members.

In this revenue ruling all insurance companies writing this type of insurance were required to be members as provided by the state. The insurance industry had been criticized for cancelling high-risk policies, therefore this was a means of minimizing public criticism of the industry.

Your organization is unlike the entity in this revenue ruling in that your membership is not made up of a specific industry but is rather businesses of any nature who have as a common denominator the need for healthcare insurance. Membership is not mandated but is purely voluntary. Not all health care providers choose to participate in your program.

Again, in Revenue Ruling 76-410, C.B. 1976-2, 155, an organization created pursuant to a state's no-fault insurance statute to provide personal injury protection benefits for residents of the state was determined to be exempt under section 501(c)(6). Every insurance company operating within the state was required to be a member. There was no competitive advantage gained by membership in the organization. These factors indicated that the organization's activities were directed to the improvement of business conditions rather than performance of particular services.

Your activities are similar to those described in Revenue Ruling 74-81, 1974-1 C.B. 135. In this ruling an organization was formed to promote, protect, and foster the business welfare and interests of persons engaged in the business of building, contracting and related activities. Membership was limited to persons engaged in the contracting trade and related industries. The organization provides its members with group workmen's compensation insurance, which is underwritten by a private insurance company. The operation of the insurance service is the organization's principal activity. In this ruling it was determined that by providing group workmen's compensation insurance for its members, the organization relieves the members of obtaining this insurance on an individual basis, resulting in a convenience in the conduct of their businesses. Therefore, the organization is rendering particular services for individual persons and is not exempt under section 501(c)(6).

Based on the court cases and revenue rulings dealing with this issue, I believe enough precedent exists to sustain the District Director's proposed denial. We briefly discussed during the telephone conference the possibility of separating the actual provision of insurance with the educational and research activities conducted by the organization. You stated that the

[REDACTED]

insurance activity was an integral part of the purpose of the organization and that would not be possible.

While I certainly feel the organization's purpose is commendable, I cannot recommend the granting of tax exempt status. Please feel free to contact me to discuss this matter further, particularly if there have been any changes to the organization's operation since our telephone conference.

If I do not hear from you by [REDACTED] I will close the case by sustaining the proposed denial. Thank you for your patience in this matter.

Sincerely,

[REDACTED]

Appeals Officer